

## Message Text

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PAGE 01 EC BRU 08916 01 OF 02 031919Z

70

ACTION EUR-12

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FM USMISSION EC BRUSSELS

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INFO ALL EC CAPITALS 1153

AMEMBASSY ATHENS

AMEMBASSY BERN

AMEMBASSY MADRID

AMEMBASSY TOKYO

LIMITED OFFICIAL USE SECTION 1 OF 2 EC BRUSSELS 8916

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TAGS: EFIN, EEC

SUBJECT: EC COMMISSION ECONOMIC FORECASTS FOR 1975 AND 1976

REFS: A. EC BRUSSELS 8794 (NOTAL), B. ROME 14231 (NOTAL),  
C. EC BRUSSELS 6232 (NOTAL)

1. SUMMARY. THE EC COMMISSION PROJECTS A MODEST UPTURN OF 3 PERCENT IN THE NINE'S ECONOMY NEXT YEAR. INCREASED EXPORTS, ESPECIALLY TO THE US, WILL LEAD THE RECOVERY. INDUSTRIAL PRODUCTION WILL CONTINUE TO BE SLUGGISH CAUSING RECORD HIGH LEVELS OF UNEMPLOYMENT. THE RATE OF PRICE INCREASE WILL CONTINUE TO DECELERATE, BUT THE CURRENT ACCOUNT BOP WILL SLIP TO A SMALL DEFICIT. THE COMMISSION BELIEVES THE EC ECONOMY IS ABOUT ON COURSE AND IT RECOMMENDS NO FURTHER EXPANSIONARY MEASURES AT THIS TIME. FRANCE AND GERMANY ARE EXPECTED TO LEAD THE ECONOMIC UPTURN WITH GROWTH RATES OF 4-5 PERCENT NEXT YEAR. THE UK AND IRELAND WILL SEE LITTLE IF ANY REAL

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PAGE 02 EC BRU 08916 01 OF 02 031919Z

GROWTH IN 1976. ITALY'S ECONOMY SHOULD BEGIN TO PICK-UP NEXT

YEAR BUT THE DETERIORATION IN ITS BUDGET DEFICIT CONCERNS COMMISSION OFFICIALS. END SUMMARY.

2. EC FORECAST: THE COMMISSION IS PROJECTING A GROWTH RATE OF 3 PERCENT IN REAL GDP IN 1976 FOR THE NINE COMPARED TO A MINUS 2.5 PERCENT THIS YEAR. THE UPTURN WILL BE RESTRAINED IN PART BECAUSE EXCESS INDUSTRIAL CAPACITY WILL DAMPEN DOWN FIXED PRIVATE INVESTMENT, AND SELECTED SECTORS WILL CONTINUE TO BE WEAK, ESPECIALLY HOUSING AND DURABLE GOODS. EXPANDED US IMPORTS WILL HELP LEAD THE EC RECOVERY; EC EXPORTS IN VOLUME TERMS SHOULD INCREASE 8 PERCENT TO THE US. THE VOLUME OF THE NINE'S WORLDWIDE EXPORTS WILL BE UP 5 PERCENT COMPARED TO A DECLINE OF 4.5 PERCENT IN 1975. IMPORTS WILL ALSO INCREASE, UP 6.5 PERCENT COMPARED TO MINUS 6.5 PERCENT IN 1975. THIS WILL CAUSE THE EC BOP ON CURRENT ACCOUNT TO DETERIORATE FROM A \$1 BILLION SURPLUS IN 1975 TO A DEFICIT OF ABOUT \$2 BILLION. THE RATE OF CONSUMER PRICE INCREASE WILL CONTINUE TO DECELERATE FROM A 12.2 PERCENT RISE IN 1975 TO 9.5 PERCENT NEXT YEAR. OPEC'S OIL PRICE INCREASE HAS BEEN INCLUDED IN THESE ESTIMATES.

3. UNEMPLOYMENT IS A GRAVE PROBLEM (SEE REF A). ITS COMMUNITY AVERAGE WILL RISE FROM OVER 4 MILLION THIS YEAR TO CLOSE TO 5 MILLION IN 1976. THERE WILL BE A SLIGHT SLACKENING OF RECORD UNEMPLOYMENT LEVELS IN THE SECOND HALF OF 1976. DESPITE THIS GROWING SOCIAL PROBLEM, THE COMMISSION BELIEVES CURRENT EXPANSIONARY MEASURES ARE SUFFICIENT. GROWING BUDGET DEFICITS LIMIT FURTHER PUBLIC EXPENDITURES; THE POSSIBILITY OF REKINDLING PRICE INFLATION ALSO RESTRAINS ADDITIONAL MEASURES. IN SUM, THE COMMISSION THINKS THE PROJECTED MODEST ECONOMIC UPTURN IS APPROPRIATE; NEXT YEAR'S EXPANSION IS CLOSE TO THE COMMISSION'S FORECAST THAT THE EC WILL HAVE AN ANNUAL GROWTH RATE OF 4-4.5 PERCENT FOR THE BALANCE OF THE DECADE.

4. FRG FORECAST: THE COMMISSION FORECASTS A SUSTAINED BUT MODERATE FRG GROWTH RATE FOR THE NEXT TWO YEARS. IT ESTIMATES THE GDP WILL FALL BY 3.8 PERCENT THIS YEAR AND RISE BY ABOUT 4 PERCENT NEXT YEAR. NO PICK-UP IN INDUSTRIAL PRODUCTION IS FORESEEN THIS YEAR BUT AN UPTURN WILL LIKELY OCCUR EARLY NEXT YEAR. (A 2 PERCENT RISE IN THE INDUSTRIAL PRODUCTION INDEX IN AUGUST AND AN INCREASE IN NEW PURCHASE ORDERS HAVE CAUSED COMMISSION OFFICIALS LIMITED OFFICIAL USE

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PAGE 03 EC BRU 08916 01 OF 02 031919Z

TO BECOME MORE CONFIDENT ABOUT AN EARLY UPTURN.) THE COST OF LIVING INDEX (COL) WILL RISE 6 PERCENT THIS YEAR AND 5.5 PERCENT NEXT YEAR. UNEMPLOYMENT WILL CONTINUE TO RISE, PERHAPS REACHING 1.5 MILLION THIS WINTER. IT WILL AVERAGE CLOSE TO 1 MILLION FOR BOTH 1975 AND 1976. THE VOLUME OF EXPORTS IS EXPECTED TO GROW 6-7 PERCENT NEXT YEAR COMPARED TO A MINUS 5 PERCENT IN 1975. THE BOP SURPLUS BASED ON GOODS, SERVICES AND FACTOR COSTS WILL FALL FROM 40 BILLION DM THIS YEAR TO 27 BILLION

NEXT YEAR. THE CONTINUED LOW RATE OF PRIVATE FIXED INVESTMENT AND THE UPWARD PUSH OF BUDGETARY FINANCING ON DOMESTIC INTEREST RATES WILL ACT AS RESTRAINTS TO THE FRG ECONOMIC RECOVERY.

5. FRANCE: THE COMMISSION'S FORECASTS FOR FRANCE ARE THE MOST BUOYANT OF THE NINE. IT FORESEES THE GDP REBOUNDED FROM A 3 PERCENT DECLINE THIS YEAR TO A 5 PERCENT EXPANSION NEXT YEAR. BARRING POSSIBLE LABOR PROBLEMS, INDUSTRIAL PRODUCTION IS EXPECTED TO REACH A 2 PERCENT GROWTH RATE BY THE LAST QUARTER. THE RISE IN CONSUMER PRICES SHOULD SLACKEN FROM AN ANNUAL RATE OF 11.6 PERCENT IN 1975 TO 9 PERCENT NEXT YEAR. THE BOP ON CURRENT ACCOUNT SHOULD REGISTER A SURPLUS OF 16 BILLION FF THIS YEAR AND SHOULD BE ABOUT IN EQUILIBRIUM NEXT YEAR. THE VOLUME OF EXPORTS IS EXPECTED TO SHIFT FROM A 3.3 PERCENT DECLINE IN 1975 TO AN INCREASE OF 5.5 PERCENT NEXT YEAR. IMPORTS, HOWEVER, WILL RISE 10.5 PERCENT IN 1975 COMPARED TO MINUS 8.3 PERCENT THIS YEAR. COMMISSION OFFICIALS SAY THE RECENT GOF'S EXPANSIONARY MEASURES ARE TOO LATE AND COULD BE COUNTER-PRODUCTIVE BECAUSE THEY WILL AFFECT THE ECONOMY WHEN IT IS ALREADY ON THE UPSWING. NEVERTHELESS, BECAUSE OF THE RELATIVE STRONG UPTURN, THE FRANC SHOULD CONTINUE TO BE STABLE AGAINST OTHER EC SNAKE CURRENCIES. THIS PROJECTION COULD BE INCORRECT, HOWEVER, IF UPCOMING LABOR NEGOTIATIONS SHOULD GO BADLY. UNEMPLOYMENT IS EXPECTED TO REACH A PEAK OF 1.2 MILLION BEFORE FALLING TO ABOUT 800,000 BY THE END OF NEXT YEAR. UNEMPLOYMENT WILL AVERAGE 880,000 THIS YEAR AND ABOUT 900,000 NEXT YEAR.

6. UK: THE OUTLOOK IS BLEAK: GDP GROWTH, MINUS 1 PERCENT IN 1975 AND ZERO NEXT YEAR. INDUSTRIAL PRODUCTION IS EXPECTED TO CONTINUE TO DECLINE UNTIL THE SECOND QUARTER OF 1976. THE GDP SHOULD BE GROWING AT A RATE OF 2-3 PERCENT BY THE LAST QUARTER OF 1976. THE COL INCREASE WILL AVERAGE 24 PERCENT AND 14 PERCENT IN 1975 AND 1976. THE COL MIGHT FALL TO A 10 PERCENT RATE BY LIMITED OFFICIAL USE

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PAGE 04 EC BRU 08916 01 OF 02 031919Z

MID-1976 AND STAY AT ABOUT THAT LEVEL FOR THE REMAINDER OF THE YEAR. UNEMPLOYMENT WILL RISE FROM A CURRENT LEVEL OF 1 MILLION TO 1.3 MILLION IN THE SECOND QUARTER OF 1976 AND THEN TAPER OFF NEAR YEAR END. THE BOP DEFICIT ON CURRENT ACCOUNT WILL BE 1.5 BILLION POUNDS IN 1975 AND 2 BILLION NEXT YEAR. DEPRESSED IMPORT LEVELS FOR THE FIRST HALF OF 1976 WILL HOLD DOWN NEXT YEAR'S DEFICIT. HOWEVER, SHOULD POLITICAL PRESSURE CAUSE HMG TO TAKE REFATIONARY MEASURES EARLY NEXT YEAR, THE 1976 DEFICIT COULD DETERIORATE SHARPLY.

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PAGE 01 EC BRU 08916 02 OF 02 040048Z

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LIMITED OFFICIAL USE SECTION 2 OF 2 EC BRUSSELS 8916

7. COMMISSION OFFICIALS BELIEVE A POSSIBLE DETERIORATION IN THE BOP DEFICIT WILL CAUSE HMG TO ACT WITH RESTRAINT. THEY ALSO BELIEVE THE POUND WILL BE ALLOWED TO DEPRECIATE FURTHER IN ORDER TO COMPENSATE FOR THE UK'S HIGHER RATE OF PRICE INFLATION THAN MOST OF ITS COMPETITORS. RESTORATION OF PUBLIC CONFIDENCE IS ESSENTIAL TO ECONOMIC RECOVERY. SHOULD HMG DECIDE TO REFLATE LATE THIS WINTER, COMMISSION OFFICIALS BELIEVE SUCH A DECISION COULD BE COUNTER-PRODUCTIVE BECAUSE IT WOULD COME TOO LATE AND WOULD UNDERCUT BUSINESS CONFIDENCE. AS IT IS, THE TOTAL PUBLIC DEFICIT FOR THIS FISCAL YEAR IS LIKELY TO REACH 11 BILLION POUNDS, AND 13 BILLION NEXT YEAR, ABOUT 7.5 PERCENT OF GNP.

8. ITALY: ALONG THE LINES OF REF B, THE COMMISSION ESTIMATES GDP GROWTH RATES OF MINUS 3 PERCENT IN 1975 AND PLUS 2-3 PERCENT IN 1976. EXPORTS ARE EXPECTED TO RISE BY 6 PERCENT IN 1976 BUT INCREASED IMPORTS WILL CAUSE THE BOP ON CURRENT ACCOUNT TO SLIP SOMEWHAT. THIS YEAR'S DEFICIT IS ESTIMATED AT 800 BILLION LIRA; NEXT YEAR'S 900 BILLION. THE COL INDEX WILL RISE AN AVERAGE OF

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PAGE 02 EC BRU 08916 02 OF 02 040048Z

17 PERCENT THIS YEAR; AND ABOUT 10-12 PERCENT NEXT YEAR, BUT THIS DEPENDS ON THE OUTCOME OF YEAR END LABOR NEGOTIATIONS. UNEMPLOYMENT SHOULD AVERAGE ABOUT 750,000 NEXT YEAR, 4 PERCENT OF THE LABOR FORCE. COMMISSION OFFICIALS SAY THERE HAS BEEN A SHARP DETERIORATION IN THE 1975 TREASURY DEFICIT. THIS DEFICIT WILL LIKELY AMOUNT TO 11 TRILLION LIRA INSTEAD OF THE 8 TRILLION TARGET. THE DEFICIT OF THE TOTAL PUBLIC SECTOR IS LIKELY TO BE 8.3 PERCENT OF GDP THIS YEAR. INSTEAD OF SHARPLY CURTAILING CURRENT EXPENDITURES NEXT YEAR, THE TREASURY DEFICIT IS NOW PROJECTED TO RISE BY 2 TRILLION LIRA IN 1976. THE CURRENT EXPENDITURE DEFICIT IS LIKELY TO REACH 5 TRILLION LIRA. THIS DETERIORATION IS DUE IN PART TO AN EROSION IN TAX RECEIPTS, IN REAL TERMS, AND TO INCREASED GOI EXPENDITURES.

9. BENELUX: BELGIUM'S ECONOMY IS PROJECTED TO GROW A MINUS 1.5 AND PLUS 3 PERCENT IN 1975 AND 1976. INDUSTRIAL PRODUCTION HAS FALLEN SHARPLY THIS YEAR AND IS NOT EXPECTED TO TURN UP UNTIL NEXT YEAR. ITS COL WILL AVERAGE A 12.2 PERCENT RISE THIS YEAR, WHICH WILL BE THE HIGHEST RATE AMONG SNAKE COUNTRIES. THIS COULD CREATE EXPORT AND EXCHANGE RATE PROBLEMS FOR BELGIUM. NEXT YEAR'S COL IS ESTIMATED TO RISE BY 9 PERCENT. UNEMPLOYMENT IS EXPECTED TO REACH 220,000 AT YEAR END, AND STAY AT ABOUT THAT LEVEL NEXT YEAR. THE BOP SURPLUS ON CURRENT ACCOUNT IS EXPECTED TO DECLINE BY ABOUT 20 PERCENT NEXT YEAR. THE NETHERLANDS' ECONOMY SHOULD GROW A MINUS 2 PERCENT IN 1975 AND PLUS 2.8 PERCENT RATES IN 1976. ITS COL SHOULD RISE 10.5 PERCENT AND 9.5 PERCENT FOR THE TWO YEARS. UNEMPLOYMENT WILL INCREASE FROM A 1975 AVERAGE OF 210 MILLION TO 250 MILLION NEXT YEAR. ITS TRADE SURPLUS SHOULD INCREASE BY ABOUT 20 PERCENT. COMMISSION OFFICIALS ARE CONFIDENT ABOUT THEIR FORECASTS FOR THE NETHERLANDS BUT ARE CONCERNED THAT BELGIAN CONSTRUCTION ACTIVITY COULD TURN DOWN AND CONSEQUENTLY AFFECT THEIR FORECASTS FOR BELGIUM.

10. DENMARK: THE ECONOMIC SITUATION SHOULD IMPROVE SUBSTANTIALLY: GNP GROWTH UP FROM MINUS 1 PERCENT THIS YEAR TO PLUS 4 PERCENT NEXT YEAR. AT THE SAME TIME THE RISE IN THE COL SHOULD CONTINUE ITS DOWNWARD TREND: 15, 9 AND 8 PERCENT IN 1974, 1975 AND 1976 RESPECTIVELY. UNEMPLOYMENT WILL ALSO BE DOWN SOMEWHAT, FROM AN AVERAGE OF 90,000 THIS YEAR TO 80,000 NEXT YEAR. THERE WILL BE SOME DETERIORATION IN THE BOP ON CURRENT ACCOUNT.

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PAGE 03 EC BRU 08916 02 OF 02 040048Z

11. IRELAND: THE COMMISSION IS CONCERNED OVER IRELAND'S ECONOMIC PROSPECTS. ITS GNP GROWTH RATE WILL FALL 3-4 PERCENT THIS YEAR AND RISE 1 PERCENT NEXT YEAR. INDUSTRIAL PRODUCTION WILL NOT START TURNING UPWARD UNTIL MID-1976. THE COL INDEX WILL AVERAGE A 21 PERCENT INCREASE THIS YEAR AND ABOUT 15 PERCENT NEXT YEAR, BUT THIS COULD BE REVISED UPWARD SHOULD UPCOMING LABOR NEGOTIATIONS SHARPLY PUSH UP WAGES. THE UNEMPLOYMENT RATE

IS CURRENTLY OVER 9 PERCENT AND IS PROJECTED TO CONTINUE AT THIS LEVEL. COUNTING PART-TIME WORKERS AND THOSE WHO ARE NOT ELIGIBLE FOR UNEMPLOYMENT INSURANCE, THE RATE IS CLOSER TO 12 PERCENT. DESPITE THIS SOCIAL PROBLEM, THE GOVERNMENT HAS LITTLE FLEXIBILITY TO TAKE FURTHER EXPANSIONARY MEASURES. THE BUDGET DEFICIT ALREADY HAS RISEN FROM 11 TO 15 PERCENT OF THE GDP; ADDITIONAL EXPENDITURES WOULD AGGRAVATE THE RATE OF INFLATION. THE BOP ON CURRENT ACCOUNT SHOULD SHOW SOME DETERIORATION NEXT YEAR BUT THIS IS NOT EXPECTED TO BE SERIOUS. COMMISSION OFFICIALS POINT OUT THAT IRELAND'S PROSPECTS IN LARGE PART DEPEND ON THE PERFORMANCE OF THE UK ECONOMIC STABILIZATION PROGRAM.

12. COMMENT. LIKE MOST OTHER FORECASTS, THE COMMISSION ESTIMATES LAST YEAR TURNED OUT TO BE HIGHLY INACCURATE (SEE REF C). COMMISSION OFFICIALS JOKINGLY SAY THAT IF THEY HAD JUST CHANGED THE SIGNS THEIR ESTIMATES WOULD HAVE BEEN FINE. THERE HAS NOW BEEN A CHANGE OF LEADERSHIP IN THE ECONOMIC FORECASTING DIVISION AND EMPHASIS IS BEING GIVEN TO UNVARNISHED ASSESSMENTS. THE ABOVE ESTIMATES ARE FOR INTERNAL COMMISSION USE ONLY. THEY HAVE BEEN DISCUSSED WITH MEMBER STATE OFFICIALS AND SOME ADJUSTMENTS WERE MADE TO REFLECT THEIR VIEWS. FURTHER ADJUSTMENTS ARE LIKELY, PARTICULARLY REGARDING THE NETHERLANDS. THE ABOVE FORECASTS COME FROM A SERIES OF CONVERSATIONS WITH COMMISSION FINANCIAL OFFICIALS WHO ARE RESPONSIBLE FOR THE INDIVIDUAL COUNTRY ANDD COMMUNITY ASSESSMENTS. AS A RESULT, THERE MAY BE SOME INTERNAL INCONSISTENCIES WHICH WILL BE WORKED OUT WHEN THE COMMISSION PUTS ITS ESTIMATES IN FINAL FORM. END COMMENT. MORRIS

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